Supreme Court, U.S.
FILED
FEB 12 1992
OFFICE OF THE CLERK

No. 91-1132

IN THE
Supreme Court of the United States

OCTOBER TERM, 1991

FREEPORT-MCMORAN INC., et al.,

Petitioners,

versus

K N ENERGY, INC.,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF OF THE INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA AS AMICUS CURIAE IN SUPPORT OF PETITIONER

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February 12, 1992

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BRIEF OF THE INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA AS AMICUS CURIAE IN SUPPORT OF PETITIONER

On behalf of its member companies, the Independent Petroleum Association of America submits this brief as *amicus curiae* in support of the petition by Freeport-McMoRan Inc. for a writ of certiorari to review the decision of the United States Court of Appeals for the Tenth Circuit, reported at 942 F.2d 765 (1991).[1]

INTERESTS OF AMICUS CURIAE

The Independent Petroleum Association of America ("IPAA") is a trade association that represents independent oil and gas producers in the United States. IPAA has approximately 5,500 members, and IPAA's mem-

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[1] The petitioners and respondent have consented to the filing of this brief. The letters granting their consent have been filed with the Clerk of the Court.

bers produce the vast majority of natural gas in the United States.

IPAA's members are parties to a broad variety of contracts used to conduct their business. These include leases, exploration agreements, farmout agreements, drilling agreements, pooling agreements, unitization agreements, operating agreements, balancing agreements, and natural gas sales agreements.

Independent producers rely on these contracts, and their application under state law, in making the large capital investments required to explore for and develop natural gas reserves. Because the Tenth Circuit's decision, establishing a new federal rule of contract law, could have an extremely disruptive impact on the way that IPAA's members conduct and structure their business transactions, IPAA has a significant interest in this Court's review of the decision below.

STATEMENT

Freeport-McMoRan Inc. ("Freeport"), et al., the petitioners here and plaintiffs below, obtained a judgment in their favor in the United States District Court for the District of Colorado after a full trial on the merits in November 1988. Subject matter jurisdiction was based on diversity of citizenship. Relying on extensive extrinsic evidence, the district court found that a provision in a natural gas sales contract allowing the seller to redetermine the price to the highest price paid for gas "sold under similar terms and conditions" was not intended to exclude prices paid for regulated gas.

A panel of the Tenth Circuit reversed the judgment of the district court, ruling that the addition of a party after the suit had been filed destroyed diversity jurisdiction. The Supreme Court reversed the Tenth Circuit, *Freeport-McMoRan Inc. v. K N Energy, Inc.*, __ U.S. __, 111 S.Ct. 858 (1991).

On August 19, 1991, the same panel of the Tenth Circuit reversed the district court again. The appellate court held that the "use of 'terms'," in the contract's redetermination provision referring to gas "sold under similar terms and conditions," is "not a synonym nor interchangeable with 'conditions'." App. p. A-7. On the basis of this distinction, the court concluded that deregulation "was a 'term' of the sale" although it was not a "condition" of the sale. App. pp. A-7, A-8.

As in its previous decision, the Tenth Circuit has ignored the settled boundaries delimiting the power of a federal court sitting in diversity. The court has, in effect, created a federal rule of contract law distinguishing between "terms" and "conditions" regardless of the parties' actual intent. The holding not only conflicts with the decisions of this Court and of another Circuit, but also defeats the parties' expectation that state law, which does not recognize the Tenth Circuit's distinction, would govern the construction of their contract. This Court should undo the mischief by granting the petition or, as it did previously, correct the error by summary reversal.

REASONS FOR GRANTING THE WRIT

This Court should review the decision below for several reasons. *First,* the Tenth Circuit's decision conflicts with the settled rule that there is no federal general common law.

Second, the decision creates serious uncertainty in the enforcement of contracts, which frequently use the words "terms and conditions" or similar phrases.

I. The Tenth Circuit's Decision Directly Conflicts With The Settled Rule That There Is No Federal General Common Law.

In *Erie R. Co. v. Tompkins,* 304 U.S. 64 (1938), this Court held that "[e]xcept in matters governed by the Federal Constitution or by Acts of Congress, the law to

be applied in any case is the law of the state." 304 U.S. at 78. In the construction of gas purchase contract clauses very similar to the dispute at issue here, this Court has noted "that the interpretation of the favored nations clause raises only questions of state law." *Arkansas Louisiana Gas Co. v. Hall,* 453 U.S. 571, 579 n. 9 (1981). The Tenth Circuit's decision, tacitly creating a federal common law rule of contract construction, simply cannot be reconciled with the teaching of *Erie* and *Arkansas Louisiana.*

The Tenth Circuit's decision also conflicts directly with the Fifth Circuit's holding in *Pennzoil Co. v. FERC,* 645 F.2d 360 (5th Cir. 1981), cert denied, 454 U.S. 1142 (1982). *Pennzoil* held that the Federal Energy Regulatory Commission must apply state law in determining whether gas purchase contracts authorize collection of federal ceiling prices. *Pennzoil* also explicitly held that "the federal legislation and regulation of this area does not directly address the interpretation of gas purchase escalation provisions." 645 F.2d at 385.[2] To resolve this conflict between the Circuits as well as to deter the very type of forum shopping *Erie* was designed to prevent, this Court should review the decision below.

II. The Tenth Circuit's Holding Will Cloud Numerous Contracts And Cause Turmoil.

The "terms and conditions" phrase which is the subject of the Tenth Circuit's new rule of contract interpretation is rife in gas purchase contracts[3] and other contracts used in the oil and gas industry. These contracts

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[2] Reliance on substantive state law is all the more appropriate because all federal price controls on "first sales" of natural gas will be phased out by January 1, 1993. See Wellhead Price Decontrol Act of 1989, Pub. L. 101-60, 103 Stat. 157 (July 26, 1989).

[3] See, e.g., D. JOHN, N. HENGERER & P. ESPOSITO, NATURAL GAS CONTRACTS, §§ 58.023, 58.025, and App. I (1984) (model contract provisions); *Superior Oil Co. v. Western Slope Gas Co.,* 604 F.2d 1281, 1284 (10th Cir. 1979).

typically involve millions of dollars of revenues and affect the delivery of a commodity which serves millions of residential and commercial end-users. Hence, the Tenth Circuit decision to, in effect, supplant state law in favor of that court's newly invented, nebulous distinction between "terms" and "conditions" will not only cloud the administration of numerous contracts essential to the day-to-day operations of the oil and gas industry. The disruption caused to this critical industry through the uncertainty and litigation generated by the Tenth Circuit will ultimately be felt across the nation by those whom the industry serves — business and household alike. Review of the decision below is therefore indispensable in order to restore the contract certainty upon which this industry and its customers rely.

CONCLUSION

For the foregoing reasons, this Court should either grant the petition and review the decision below on the merits or summarily reverse this Tenth Circuit panel again.

Respectfully submitted,

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